BEFORE THE AGRICULTURAL MARKETING SERVICE
UNITED STATES DEPARTMENT OF AGRICULTURE

DAIRY PRODUCT MANDATORY REPORTING	)
Interim Final Rule and Opportunity for	) Doc. AMS-07-0047
Submitting Comments	)
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COMMENTS SUBMITTED ON BEHALF OF THE ALLIANCE OF WESTERN MILK PRODUCERS

I. SUMMARY OF POSITION

These comments are submitted on behalf of The Alliance of Western Milk Producers (‘Alliance”) in response to the July 3, 2007 Federal Register publication by the Agricultural Marketing Service (“AMS”), an agency of the United States Department of Agriculture (“USDA”), of an Interim Final Rule regarding Dairy Product Mandatory Reporting regulations. The focus of these comments is on the portion of the Interim Final Rule that addresses the reporting of nonfat dry milk and in particular the issue of which sales of nonfat dry milk should be reportable in reporting to USDA’s National Agricultural Statistics Service (“NASS”). Alliance respectfully disagrees with AMS’ Interim Rule provision that limits the reporting to sales of nonfat dry milk where the price is fixed by contract for over 30 days. This has the obvious effect of excluding all long term contract sales from reporting. The resulting weighted price is therefore missing a significant volume of product. The NASS price so calculated is then used to determine the milk price that the processor of the nonfat dry milk will be required to pay his producers. In volatile market conditions, which certainly are the case now, no processor can afford the risk if making long term contract sales if he is not assured that the same price will be part of the calculation of his cost of milk. The processor, whose profit is already limited to the established make allowance, will simply not enter into long term export contracts. The 30 day rule thus has an impact on the pricing reported instead of being a report of prices. Formula pricing in this instance creates a situation where the reporting process itself impacts the pricing result. *All sales of qualifying product whether sold on the spot market or via long term contracts should be included in the NASS reports.* The overwhelming reason for this is to assure all processors that all of their sales will be included in determining the cost of the milk they are processing.

ALLIANCE OF WESTERN MILK PRODUCERS

The Alliance of Western Milk Producers is an association of Cooperatives and has as its members California Dairies, Inc (CDI); Dairy Farmers of America – Western Council (DFA) and Humboldt Cooperative Creamery (HCC). The California members of these three organizations produce a bit more than 63% of the milk produced in California. In the context of this comment it is useful to note that our members process at least two-thirds of the nonfat dry milk (NFDM) produced in California and that California plants produce well over 50% of the NFDM produced in this country. One of our members, CDI, is nearing the completion of a new NFDM plant in Visalia which will have a capacity of five million pounds of milk per day.

The concepts presented in this letter were approved by the Board of Directors of the Alliance at the July 23, 2007 meeting and were presented at the California Department of Agriculture hearing on August 28, 2007. That hearing was called to consider proposed changes to the California Weighted Average Price ("CWAP") which the price used on determining the 4a price in our state. The concepts presented at the California hearing apply equally to the issue we are addressing in this comment.

Changing world

In the past few years major changes have been occurring in world dairy trade. Foremost among those changes is the gradually increasing relative wealth of the citizens of the developing nations in many parts of the world, particularly in Asia. With this has come increasing demand for dairy proteins. At the same time the European Union (EU) has trimmed what had been a very generous dairy program and they are no longer participating in world markets with large volumes of subsidized product. It does not appear they will ever reinstitute a similar program. The drought in Australia has been going on for years and it will be a long time before they can recover. In spite of high prices Australia projects decreases of milk production in the coming year.

These factors plus others create an opportunity for California dairymen to produce and market NFDM world wide. We have the strong belief that the future of California's dairy industry lies in export sales to the West. Interestingly, and precisely on point, the balance of the United States would find it difficult to participate in export contracts because of the 30 day rule applied by NASS.

The demand for NFDM is high and the prices are attractive. All indications are that this demand will continue for quite some time, mostly because there are few other places in the world that can respond. The current high milk prices enjoyed by producers are driven almost exclusively by the world wide demand for milk proteins.

But being a large-scale and long-term marketer of dairy products to the world market is new to our state and our country. Accordingly great care must be taken to insure that our regulations are flexible enough to allow NFDM processors to engage in business transactions the will enhance our country as a reliable major provider of NFDM (and other dairy proteins). Regulations to the contrary can only inhibit this evolution and injure dairy producers and NFDM processors. The world - with these high prices - is asking us to supply it with product, our producers are responding and our state - and country - needs to have a regulatory system that allows a sensible economic response.

Review of other options

After review, the Alliance finds that the procedures put together in 1973 – 34 years ago – are still a better option for California than any of the other proposals. The basic idea behind the California Weighted Average Price (“CWAP”) was to use the **actual** values received by California plants for standard NFDM as the basis for determining what those plants paid for their milk. Looking back over the past one third of a century, one has to be impressed by how well this approach has worked for both producers and processors.

In the California hearings proposals were put forth to limit the inclusion of contracts (to 90 days) or to match the NASS system of a 30 limit. In either case the regulations would create a regulatory environment that moves away from a system that has worked well for over three decades based on the very unusual price and market circumstances that occurred during a short period in 2007.

Similar choices have been presented to NASS. These proposals would severely limit the ability of this country to participate in export trade.

It has been proposed that all sales based on fixed contracts that are not delivered within the first 90 days of the contract signing shall not be included in the NASS prices. The use of 90 days is arbitrary and is difficult to justify. Is it the intent to limit all future contracts to 90 days or less? There are many complexities in preparing and delivering product to international accounts and we believe that limits of this sort would curtail the potential markets to which processors could deliver product. This approach assumes that long term contracts are always inferior to the prevailing market price and that the price received after 90 days will always be less. That supposition is not and cannot be true. Additionally, this proposal has the unintended effect (which we think is a fatal flaw) of leaving the processor in the enviable position of being able to choose, by manipulating the delivery date, whether or not a particular contact will be included in pricing calculations. Our view is that <u>all</u> sales of the properly defined commodity products should be included whether sold on long term contracts or as spot sales.

NASS prices as presently constructed create a disincentive to export on the basis of long-term contracts because for in nearly all cases the value of the export sales will not be included in the price series used to establish the value of the milk. It will be a rare event that any powder sold on a long-term contract will be reported to NASS because it nearly always takes longer than that (often twice as long) to get all the approvals and testing needed to actually begin shipping product.

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Consequences of Improper Regulations

There are two readily apparent consequences of creating regulations that are out of touch with the business environment in which export transactions are made:

- potential sales to export trade will not proliferate but will instead fail to materialize and more product will have to be marketed domestically, and

- the resulting overabundance of domestic supply will negatively impact prices.

Closing

We strongly believe that all long term contracts for commodity NFDM should continue to be included in CWAP reporting and so testified. If NASS continues to exclude all long term contracts, the impact will be that all export sales will occur from California only. The function of NFDM plants in a regulated environment is not to be risk taking profit centers. The function is to process milk as efficiently as possible into a storable stable long lived product and in doing so provide the extremely valuable service of balancing markets. Economic logic dictates that whatever limit is set by NASS (or CWAP) will be the limit to the time commitment of export contracts. NFDM plants must be able to expect the regulated price to be set based upon their actual sales of the product produced. If exports are excluded (as they for all practical purposes currently are with the NASS 30 day rule) then plants living with that rule will not, because of the size of the risk compared to their limited profit potential, be able to participate in any long tern contracts.

There is before us a chance to foster the marketing of products of the United States to the world. The demand for milk protein has made 2007 a very unusual year that has presented novel circumstances, price levels and price relationships. So far this set of events is working out well for California and the California industry is poised to seize that opportunity. There is no good reason to exclude the rest of the country. NASS procedures have already made the error of failure to include long term export sales. The procedure should be changed to include long tern export sales.

Respectfully submitted,

William C. Van Dam, CEO
Alliance of Western Milk Producers.